

NATIONAL CREDIT UNION ADMINISTRATION

OFFICE OF INSPECTOR GENERAL

**YEAR 2000
READINESS STATUS OF
CREDIT UNION VENDORS**

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Frank Thomas

**FRANK THOMAS
INSPECTOR GENERAL**

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Introduction

This is the sixth of the Office of Inspector General's (OIG) series of reports addressing the Year 2000 (Y2K) computer problem as it relates to the National Credit Union Administration (NCUA) and federally insured credit unions (FICUs). This report addresses the OIG review of federally insured credit unions' information system vendors and their progress and affect on credit union ability to prepare for the year 2000.

Because of the time critical nature of the Y2K problem, and in order to provide the NCUA Board with timely information, we are not making formal recommendations or asking for a written response.

Background

The NCUA supervises 11,019 natural person credit unions 6,799 federally chartered and 4,220 state chartered. Approximately 92 percent of these credit unions were identified as using EDP vendor products for core processing (share and loan systems). In August 1997, NCUA issued a letter to all known Information System Vendors (primary ISVs) that provide service to credit unions. This letter requested the vendors to complete a Y2K questionnaire and also mentioned plans to have a vendor conference in late 1997. On March 20, 1998, the Examination Parity and Year 2000 Readiness for Financial Institutions Act was enacted giving NCUA and the Office of Thrift Supervision examination authority over ISVs, similar to other financial institution regulators, to assure the safety and soundness of the nation's financial institutions.

Prior to the enactment of the Examination Parity Act, ten ISVs were reviewed by NCUA and its contractor on a voluntary basis. These ten ISVs served approximately 55 percent of federally insured credit unions. After the enactment of the Examination Parity Act, NCUA and its contractor performed an additional 36 ISV reviews. These 46 ISV reviews covered approximately 86 percent of federally insured credit unions. All of these reviews were of primary ISVs covering core processing systems (primarily share and loan systems). The scope of the reviews was to determine the vendors' Y2K process and status to date. The scope was NOT to certify vendor Y2K compliance. The reports are reviewed by NCUA and provided to the vendor for comment. Upon finalization of the report, it is distributed to NCUA regional offices, state supervisory authorities and credit union vendor clients. In addition, an executive summary is posted on the NCUA website. The first 10 reviews performed were not distributed and not posted on the NCUA website, since they were not performed under the Examination Parity Act. These reports were summarized as to their results via an NCUA Letter to Credit Unions.

Other federal financial institution regulators have performed various EDP reviews which relate to Y2K issues under direction of the Federal Financial Institutions Examination Council (FFIEC). The federal member agencies, except NCUA, have performed these reviews. Most of these reviews, as they relate to credit unions, are of third party vendors (third party ISVs such as credit card processors etc.) Agencies in charge (AIC) perform the reviews and write the reports. The FFIEC distributes the reports to member agencies, such as NCUA. NCUA reviews the reports

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and distributes the reports, if there is no distribution restriction, to NCUA regional offices, state supervisory authorities and credit union vendor clients. As of October 13, 1999, 257 FFIEC reviews had been performed.

The NCUA, in addressing potential Y2K problems in FICU information systems, adopted milestone dates for natural person and corporate unions to accomplish specific Y2K tasks. The purpose of the milestone dates was to ensure credit union information systems were ready to function in a timely manner. Benchmark milestone dates were developed to address awareness, assessment, renovation, validation/testing, and implementation phases. In early 1998, NCUA established a policy of providing waivers or extensions to the milestone dates. Waivers and extensions have been granted for individual credit unions and blanket waivers for some credit unions with common information system vendors. If credit union remediation efforts were not performed in a timely manner in accordance with the milestone dates and waivers, the NCUA could take administrative action against the credit union because of unsafe and unsound practices. The milestone date for system renovation completion was January 31, 1999, for testing completion June 30, 1999, for substantially implementation July 31, 1999, and for final implementation by September 30, 1999. No milestone dates had been established by NCUA for ISVs. Through October 31, 1999, NCUA had approved blanket waivers on 13 vendors.

Beginning in 1998, NCUA required all credit unions to file a calendar quarterly report with NCUA. These quarterly reports, essentially, provided the status of the credit union's critical systems in the Y2K phases as reported by the credit union. These reports only listed the primary vendor. These quarterly reports were reviewed by the examiner in charge (NCUA or state), forwarded to the appropriate NCUA regional office for review and finally forwarded to the Office of Examination and Insurance (E&I) for review and database establishment. As of September 30, 1999, all credit unions were 100 percent renovated, as reported by the credit unions. And 99.97 percent of all federally insured credit unions were fully implemented, as reported by NCUA.

Objectives

Our objectives were: (a) to determine the Y2K status of credit union system vendors and (b) to determine what action NCUA was taking to ensure that vendors are making satisfactory progress in providing renovated systems to its credit union clients.

Scope and Methodology

This review was of limited scope and was not performed under yellow book audit standards. However, we did perform the following review procedures in meeting our review objectives:

NCUA Primary ISV reviews:

- Reviewed agency guidance regarding ISV vendor reviews
- Interviewed E&I staff regarding vendor review processes, procedures and results
- Reviewed a non-statistical judgmental sample of vendor review reports and executive summaries

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- Reviewed postings per NCUA website for vendor reviews

FFIEC ISV reviews:

- Reviewed NCUA guidance regarding vendor reviews
- Interviewed E&I staff regarding NCUA review processes, procedures and results
- Scanned listing of FFIEC reports for noted problem issues
- Inquired of E&I staff regarding noted FFIEC reports which resulted in unsatisfactory or needs improvement ratings

NCUA Approved Blanket Waivers:

- Reviewed agency guidance regarding blanket waivers
- Interviewed E&I staff regarding blanket waiver processes, procedures and reasons for blanket waiver issuance
- Reviewed blanket waiver documentation supporting the need for approval

March 31, 1999 Credit Union Quarterly Reports:

- Obtained a listing of 100 percent of credit unions not fully renovated as of March 31, 1999
- Inquired of NCUA regions:
 - Listing of systems not renovated (system type and vendor)
 - Reason for non-renovation
 - Action taken
 - Current status
- Analyzed quarterly reports for trends among vendors and reasons for non-renovation

Summary Analyses:

- Compared timing, action taken and status of:
 - March 31, 1999 quarterly report of non-renovated systems
 - NCUA vendor reviews
 - FFIEC vendor reviews
 - NCUA approved blanket waivers

OBSERVATIONS

NCUA has reported that substantially all federally insured credit union mission critical systems were renovated by the NCUA testing milestone of June 30, 1999. All but 48 credit unions reported that they had met the July 31, 1999 substantially implemented milestone date.

NCUA staff feel confident that the status of vendors is accurately reported due to the various programs which were put in place by NCUA regarding ISV systems. These include:

1. NCUA conducted on-site primary vendor reviews
2. FFIEC vendor reviews
3. NCUA examiner and regional office reporting of vendor problems
4. Off-site contacts as needed for problem vendors
5. Issuance of blanket waivers
6. Credit union due diligence in testing vendor products

NCUA Vendor Reviews

NCUA along with a nationally known contractor reviewed 46 primary vendors accounting for approximately 86 percent of credit union primary core systems. These reviews did not certify vendor Y2K compliance but did include a review of the vendors' Y2K plans and processes. One review was performed in 1997, 44 were performed in 1998 and one was performed in 1999. All 46 vendors reviewed were rated satisfactory.

We were provided copies of 30 reports. At the time of NCUA's review, four of those vendors were in the renovation stage, eight in testing and 18 were in the implementation stage or completed implementation. The first 10 reviews indicated that all ten were in the renovation process at the time of NCUA's review. We reviewed 19 vendor reports. Although all reports listed some considerations for vendors, 17 of those were not major concerns. We noted two vendors which were only single person operations and had no formal testing plans. We considered these to be major concerns. According to E&I, no follow-up vendor reviews have been performed to date.

As of September 1999, the NCUA website had 20 executive summaries of reports listed and referred the first 10 summary results to a distributed NCUA Letter to Credit Unions. This leaves 16 vendor review results unposted at a time when substantially all credit unions are reported to be substantially implemented. This was due primarily to delays between E&I review of the reports and receipt of vendor comments on the draft reports.

FFIEC Vendor Reviews

We reviewed a listing of 158 FFIEC vendor review reports. We noted that four vendors had noted problems causing a formal agreement with FFIEC and/or needs improvement or unsatisfactory rating. With each one of these vendors, the AIC had conducted follow-up reviews. Two of these vendors are still under written agreements with FFIEC as of October 13, 1999.

Since May 1999, the FFIEC has issued an additional 99 reports. E&I is still in the process of distributing these reports.

NCUA Approved Blanket Waivers

NCUA approved a total of 13 blanket waivers. Seven of these waivers were approved retroactive to cover milestone dates that had passed. NCUA approved these waivers to document action taken by the agency.

NCUA contacted vendors, who were covered by a blanket waiver, for information regarding the cause, status and plans on addressing the Y2K issue at hand. Nearly all of these waivers were due to testing concerns, in that test results were not available at NCUA milestone dates. However, one corporate credit union caused a blanket waiver to be issued due to slow system renovation as it related to natural person credit unions. In this regard, the corporate credit union system was a vendor system for client natural person credit unions. National and regional staff contacted the corporate and the system has since been renovated, tested and implemented.

NCUA is able to determine how many credit unions are clients of particular vendors by reviewing NCUA database information. The FFIEC provided listings of credit union clients for the vendors which they reviewed. The listing of whether any particular vendor product is a critical system was to be determined by the credit union. However, no national analysis was performed regarding how many or which credit unions should have or could be expected to apply for a waiver under the blanket authority. E&I stated the regions are responsible for such analysis, however, at least four regions do not maintain vendor client lists.

Credit Union Quarterly Reports

Our review of quarterly information reports for non-renovated systems did not identify any major trends of any vendor not being renovated. The substantial majority of non-renovated systems were due to vendor system installation scheduling and system conversions.

As of March 31, 1999, there were 287 credit unions reported as not 100 percent renovated. However, as of September 30, 1999 all credit unions reported being 100 percent renovated.

MATTERS FOR CONSIDERATION

Since NCUA has reported that 99.97 percent of all federally insured credit unions were fully implemented as of September 30, 1999, we offer no substantial recommendations. However, we encourage the following:

- Continue to post NCUA vendor reports to the NCUA website and distribute appropriately.
- Continue to distribute FFIEC reports, as appropriate
- As new vendor problems arise, if any, promptly notify affected regions, state regulators and client credit unions

